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C O N F I D E N T I A L SECTION 01 OF 02 ANKARA 007442

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TAGS: [ENRG](#) [EINV](#) [ECON](#) [PREL](#) [TU](#)

SUBJECT: ENERGY REGULATOR PESSIMISTIC ABOUT REFORM

REF: A. ANKARA 6144 (C)

[1](#)B. ANKARA 7103

[1](#)C. ANKARA 7180

[1](#)D. ANKARA 6538

(U) This cable was classified by Econcouns Scot Marciel for reasons 1.5 (b,d).

[1](#)1. (C) Summary. EconCouns met with Energy Market Regulatory Authority (EMRA) President Yusuf Gunay for an update on energy issues, including the pending Petroleum Law, electricity market reform, gas market reform, and Build-Operate-Transfer disputes. Gunay had mixed feelings about the Petroleum Law, which gives EMRA the authority to regulate the market and requires all players to apply for licences. Gunay believes that the government is using the Petroleum Law to stack EMRA's board with anti-reformists and undermine the board's autonomy so that all energy policies would be determined solely by the Ministry of Energy at the Prime Minister's behest. In his view, Foreign Minister Gul is the only Cabinet member who supports energy market reform fully and understands that EMRA should remain independent. He was not hopeful that the pace of energy market liberalization would pick up, given the government's tight grip on policy issues and its insistence on keeping utility prices low. Gunay stressed that privatization in the energy sector would be stalled because the GOT continues to block the implementation of regional electricity tariffs and protect the State Pipeline Company's (BOTAS) monopoly. (End Summary)

[1](#)2. (C) On December 2, EconCouns and Econspecialist met with the EMRA's President Yusuf Gunay for an update on energy market reform. Gunay was especially concerned about the pending Petroleum Law, which would necessitate a restructuring of the regulatory authority to add oil to its portfolio, in addition to electricity and natural gas. If the legislation is approved in its current form, two new members would be added to EMRA's board for a total of nine members. However, the term of service for two of the current board members has expired, so the GOT would effectively be appointing four new members to EMRA's board. Gunay believes that a nine-member board would be ineffective and has appealed to the Council of Ministers to change the draft legislation and maintain the seven-member board before the final vote. Turkey's petroleum market is valued at about \$25 million in terms of volume, and the pending Petroleum Law will require all market players to apply to EMRA for licences.

[1](#)3. (C) Other contacts in the energy sector have told us that the GOT is manipulating EMRA's board by replacing two of the most effective members, Vice President Ali Turkoglu and Middle East Technical University academician Osman Sevaioğlu on the pretext that their term of office has expired. EMRA's board were all appointed at the same time for 6 years duty. Since these are the first board members, EMRA's internal regulation requires two members, excluding the President, be replaced every year through random selection. The new members will then serve for 6 years consecutively. Our contacts believe that the GOT ignored the random selection process and forced out Turkoglu and Sevaioğlu.

[1](#)4. (C) Gunay said that the government wants to control the energy sector, and that the Prime Minister does not want EMRA to regulate the sector. As a direct consequence, Gunay said that EMRA is very careful and transparent with all of its activities to avoid mistakes, which would give the GOT an excuse to dismantle the board. Reftel (A) discussed EMRA's concern that Petroleum Law would give the GOT an opportunity to appoint anti-reformists to EMRA's board and unduly influence EMRA's regulatory activities. Gunay said that Foreign Minister Gul is trying to be helpful and Finance

Minister Unakitan to a lesser extent.

15. (C) Gunay was even less sanguine about the implementation of a regional tariff regime, which remains key to privatization of energy distribution systems. Although a regional tariff regime is an essential part of a functioning electricity market to attract investors and yield lower electricity prices over time, the GOT continues to block implementation to curry favor with voters (ahead of local elections scheduled for March), many of whom would initially face higher electricity prices (reftel A). Turkish Treasury and the Energy Ministry are required to prepare a support scheme to ease the transition for consumers in rural areas; however, EMRA told us that both have refused to cooperate. Gunay believes that the government is unlikely to change its attitude, and this issue is no longer on the government's agenda. Nonetheless, he expects that EMRA will be blamed when there are no new market participants and energy privatization stalls.

16. (C) Under the proposed regional tariff system called for in the Electricity Law, 78 percent of industrial users would face lower electricity costs. In anticipation of these lower costs, the Izmir Chamber of Industry has filed three complaints to the Danistay (Court of State) to force EMRA to introduce the regional tariff system, following delays in August, September, and October. Currently, the customers in Izmir are using the national tariff system like all other consumers in Turkey, which means that they are paying for electricity leakages in other less developed parts of Turkey. Given Izmir's industrial development and complex electricity distribution network, the cost-reflective regional tariff system, would lower costs significantly. According to EMRA officials, the Danistay's ruling would be binding for EMRA, and Izmir would be able to use the regional tariff system over the GOT objections. If the court rules in favor of ITO, this would open the door for other larger cities to follow suit.

17. (C) Gunay was pessimistic about gas market liberalization, especially because BOTAS has not taken the appropriate steps to transfer shares to the market and permit private entrants to enter the gas market. BOTAS is legally obligated to transfer 10 percent of its market share annually to reduce its total share to 20 percent by 2009 (reftel D). EMRA is planning to fine BOTAS for non-compliance because BOTAS remains unwilling to consider EMRA's proposals to facilitate gas market liberalization. However, EMRA officials told us that the Energy Ministry plans to amend the Natural Gas Law to give BOTAS a way out. According to Gunay, the GOT views the gas release contracts in terms of lost profits for BOTAS, not in terms of eliminating a monopoly and establishing a free market.

18. (C) On BOTs (reftels B and C), Gunay said that the Energy Ministry is working with the companies to reach a solution. He said that they are closer to a buy-out option. He hinted that the BOT companies have told the energy authorities that the USG supports the buy-out option. EconCouns emphasized to Gunay our policy to encourage both sides to reach a fair solution, given the negative ramifications for Turkey's reputation as a host for foreign investment.

19. (C) Comment. The GOT lacks the political will to move forward with energy market reform. The GOT has shown its determination to curb EMRA's authority by circumventing the normal procedures to replace EMRA board members. Given the fallout from the BRSA's handling of Imar Bank and the ongoing investigation of BRSA's former chair, EMRA's board members are likely to be more cautious, which could slow the reform process further. Both industry and consumers are benefitting in the short run with the GOT's policy not to raise utility prices for one year; however, the GOT cannot freeze prices for an extended period. End Comment.

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